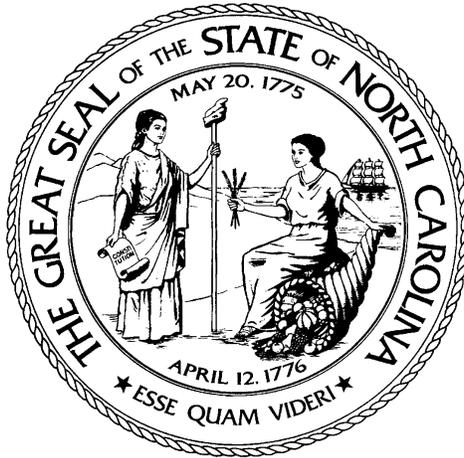


**JOINT COMMITTEE ON EXECUTIVE
BUDGET ACT REVISIONS**



**REPORT TO THE
2004 SESSION OF THE
2003 GENERAL ASSEMBLY
OF NORTH CAROLINA**

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JOINT COMMITTEE ON EXECUTIVE BUDGET ACT REVISIONS

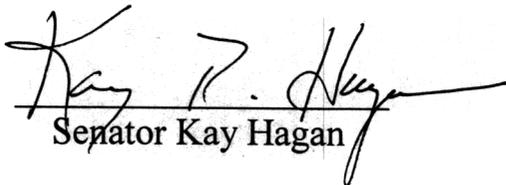


March 29, 2004

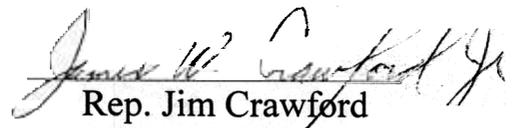
The Honorable Beverly Perdue, Lieutenant Governor
The Honorable Marc Basnight, Senate President Pro Tempore
The Honorable James B. Black, Speaker of the House
The Honorable Richard T. Morgan, Speaker of the House

The Joint Committee on Executive Budget Act Revisions submits to you for consideration its 2004 final report on Executive budget act revisions. The report was prepared by the Committee pursuant to 6.12(a) of Session Law 2003-284.

Respectfully submitted,


Senator Kay Hagan


Rep. Rex Baker


Rep. Jim Crawford

Cochairs
Joint Committee on Executive Budget Act Revisions

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2003-2004**

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PREFACE

The Joint Committee on Executive Budget Act Revisions was established in Section 6.12(b) of S.L. 2003-284 (2003 Appropriations Act). That legislation directed the Joint Committee to "consider contemporary financial management practices" and to recommend any changes in the Executive Budget Act that would "modernize and improve" the State's budget processes. The Joint Committee has spent numerous hours doing an exhaustive review of the State's budget process and the Executive Budget Act and will continue to meet in the next few weeks to incorporate its recommendations into legislation for consideration by the General Assembly in the 2004 Regular Session.

The need for a review and possible recodification of the Executive Budget Act grew out of discussions within the Joint Appropriations Committee during the 2003 legislative session. Speculation about the merits of zero-based budgeting, concern about expenditures treated as "off-budget", dissatisfaction with the role of the legislature in the approval of budget transfers, and unease about proliferation of special revenue funds were among the items that prompted members to read the State's principal budget law more carefully.

Unfortunately, the statutes regarding the State's budget do not provide the clarity that these topics deserve. The Executive Budget Act, while quite an achievement at the time it was first enacted, is no longer a coherent legal framework for budget development and administration, whether by the Governor in his capacity as director of the budget or by the General Assembly in its responsibility to consider competing needs and appropriate limited resources among those needs. Much of the core language in the Act dates to 1925. The core is overlaid with hundreds of amendments that have been fashioned piecemeal to address changing

political demands, changing legal demands, and changing governmental structure. The product makes for very difficult reading. In fact, for a number of years the North Carolina Institute of Government has periodically issued an interpretive booklet entitled The Executive Budget Act Topically Arranged, where the jumbled sections are presented in a more logical order.

Several studies of the State's budget processes and the Executive Budget Act have been undertaken in past years. The General Assembly's Government Performance Audit Committee (GPAC), concluding intensive study in 1992, identified numerous flaws in the State's fiscal management practices. Many of these, in particular the lack of a viable capital improvements planning process, owed directly to inadequacies of the Executive Budget Act. The Joint Select Fiscal Trends and Reform Study Commission reported the conclusions of one of its subcommittees in 1993: "Based on its work, the Subcommittee determined that the Executive Budget Act, first enacted in 1925 and modified in a 'piecemeal' fashion through the years, no longer provides a clear and logical statutory scheme outlining the State's budgetary process." Another study committee on the Executive Budget Act was appointed in 1995, and while it spent the bulk of its time crafting a constitutional amendment to establish legislative review of mid-year budget adjustments, cited in its report the need for a complete revision to make the Act readable and coherent. However, to date few of these suggestions have been implemented. Recognizing that many of the findings and recommendations from these past studies are still valid and should receive serious consideration, the Committee members have reviewed and profited from the work of its predecessors.

In addition to a review of past studies, Committee members reviewed the history of the Executive Budget Act back to its origins; heard knowledgeable staff from both the Executive Branch and the Legislative Branch explain current budget management practices; solicited input

from experts outside State government and studied material from the National Conference of State Legislatures characterizing budgeting and appropriations machinery in other states. As noted above, the Joint Committee will continue to gather information and receive expert counsel, and plans to recommend legislation for consideration by the General Assembly in the 2004 Session.

The Joint Committee has been guided in this exercise by three principal objectives. The first is to simplify, organize, and where necessary restate the substance of the current law so that it can be more easily understood and more accurately applied. The second is to discard out-dated concepts and replace confusing terminology with modern accounting definitions. Finally, the Committee intends to refocus the constitutional requirement for "acts of appropriation" to assure that legislative review extends beyond the General Fund to encompass the expenditure of all state Governmental and proprietary funds.

MINUTES

January 13, 2004

The Joint Committee on Executive Budget Act Revisions met Tuesday, January 13, 2004, at 8:30 a.m. in room 612 of the Legislative Office Building. Co-chair, Representative Rex Baker, presided. Three Senate members and four House members were in attendance.

The Co-chair called the meeting to order and acknowledged the staff members and the sergeants-at-arms.

Six presentations were given to the Committee:

1. *Introduction of the Executive Budget Act (Article 1 of Chapter 143 of the General Statutes revised through 2003 Regular Session) Committee Charge* – Emily Johnson, Bill Drafting Division

SESSION LAW 2003-284 (HOUSE BILL 397)

AN ACT TO APPROPRIATE FUNDS FOR CURRENT OPERATIONS AND CAPITAL IMPROVEMENTS FOR STATE DEPARTMENTS, INSTITUTIONS, AND AGENCIES, AND FOR OTHER PURPOSES, AND TO IMPLEMENT A STATE BUDGET THAT ENABLES THE STATE TO PROVIDE A SUSTAINABLE RECOVERY THROUGH STRONG EDUCATIONAL AND ECONOMIC TOOLS.

The General Assembly of North Carolina enacts:

PART VI. GENERAL PROVISIONS

JOINT COMMITTEE ON EXECUTIVE BUDGET ACT REVISIONS

SECTION 6.12.(a) There is created a Joint Committee on Executive Budget Act Revisions. The Committee shall be composed of 8 members, four of whom shall be Representatives who are members of the Appropriations Committee appointed by the Speaker of the House of Representatives and four of whom shall be Senators who are members of the appropriations Committee appointed by the President Pro Tempore of the Senate. The speaker of the House of Representatives shall designate one member as cochair and President Pro Tempore of the Senate shall designate one member as cochair. The Committee shall meet upon call of the cochairs.

SECTION 6.12.(b) The Committee shall consider contemporary financial management practices in reviewing the current Budget process. The Committee shall recommend any changes to the Executive Budget Act that are needed to modernize and improve the processes of budget preparation, budget adoption, budget execution, and program evaluation. The Committee shall report its recommendations to the 2003 General Assembly on or before April 1, 2004.

SECTION 6.12.(c) The Legislative Services Office shall assign professional and clerical staff to assist the Committee in its work. Members of the Committee shall receive per diem, subsistence, and travel allowances in accordance with G.S. 120-3.1, 138-5, or 138-6, as appropriate.

2. *Executive Budget Act, Overview and History* - Lynn Muchmore, House Budget Development, Fiscal Research Division
3. *NC's Budgeting Policies, Practices and Preparation Requirements* - Mona Moon, Senate Budget Development, Fiscal Research Division

The Committee recessed at 11:30 a.m. for lunch and returned at 12:30 p.m. to resume hearing presentations.

4. *Budget Preparation Methodologies* - William C. Rivenbark, Assistant Professor, UNC Institute of Government
5. *Budget Preparation-OSBN Perspective* - Charles Perusse, Deputy State Budget Officer, Office of State Budget and Management
6. *Budget Preparation-An Agency Perspective* - Tracy Little, Deputy Secretary of Administration, Department of Corrections, and Barbara Baker, Chief Budget and Procurement Officer, Department of Corrections

A question and answer session was held after each presentation. Representative Baker recognized and welcomed Speaker Morgan who attended the meeting.

In conclusion, a committee discussion was held to decide what direction to take in updating and revising the Budget Act. It was suggested that the staff formulate recommendations from the 1993, 1995, and 1996 summaries of the Act and specifically explain the Act to members. A request was made that staff present relevant issues that should be addressed by the members of the Committee and any available model legislation of The Executive Budget Act created by other states that would be informative. The main concern of all the members was how to approach the task and what the main priorities would be in revising and updating the Act. All agreed that structure and methodology were the keys.

Co-chair Baker adjourned the meeting at 4:00 p.m.

March 9, 2004

The Joint Committee on Executive Budget Act Revisions met Tuesday, March 9, 2004, at 8:30 a.m. in Room 421 of the Legislative Office Building. Co-chair, Senator Kay Hagan, presided. Four Senate members and three House members were in attendance.

The Co-chair called the meeting to order and acknowledged the Committee members and staff members.

The first presentation on the agenda was *Legislative Consideration of the Budget: An Overview of Requirements and Practices*, presented by Jennifer Hoffman, Fiscal Research Division. The presentation reviewed how the Executive Budget Act influences the Governor's recommended budget and the roles of the General Assembly, the Appropriations Committee, full Appropriations co-chairs, and subcommittees in submitting a budget. Questions and discussions were entertained following the presentation and the Committee members were in full agreement that the current Executive Budget Act contains many inconsistencies.

The Committee was fortunate to have Mr. Ron Snell, Director of Economic, Fiscal and Human Resources, National Conference of State Legislatures on the agenda as the second presenter. He discussed *The North Carolina Legislative Budget Process: Comparisons With Other States*. Mr. Snell took questions relevant to how North Carolina compares with other states, such as Texas, Florida, and Oklahoma.

After a brief break, a panel discussion on *Legislative Consideration and Adoption Issues* was held. Those participating on the panel were: Dr. Charlie Coe, Professor, Political Science and Public Administration, North Carolina State University; Moderator Ran Coble, Executive Director, NC Center for Public Policy Research; Dan Gerlach, Senior Policy Advisor, Office of the Governor; and John Hood, President of the John Locke Foundation.

Dan Gerlach feels the most important practice or issue related to legislative consideration and adoption of the budget is to get the budget done as early as possible. The Legislature needs to explore the timeliness of getting a budget. Also, the Legislature needs to recognize the issues important to the state.

Ran Coble gave an overview of areas that need improvement:

1. Differences in line item and program budget.
2. Expansion versus continuing budget.
3. Not passing the budget by the deadline or end of the fiscal year.
4. Special provisions.
5. Number of earmarked funds.
6. Avoiding use of nonrecurring money allocated to programs occurring.
7. The need for a long-range capital improvement plan.
8. Openness—give the public and rank and file more time to absorb the long document.
9. Benchmarks—have incentive programs that reward those state agencies that are performing well under the benchmarks.
10. Have the budget out 48 to 72 hours before going to Chambers.

John Hood addressed the issue of reforming the budget process in North Carolina, stating “There is no more important function carried out by the General Assembly and the Governor each year than fashioning and implementing a state budget that addresses the core functions of government, meets the State's highest priorities, and expends the taxpayers' money in an efficient and effective manner.” He does not feel that the current process meets these tests.

The panel interacted with members of the Committee pertaining to additional questions and explanations from the members.

After a break for lunch, the Committee reconvened at 1:00 p.m. to hear a presentation of *Potential Revisions to the Executive Budget Act, Preparation of the Governor's Recommended Budget* by Mona Moon and *Legislative Consideration and Adoption of the Budget* presented by Marilyn Chism, Fiscal Research Division. A discussion period followed.

Co-chair Hagan adjourned the meeting at 4:00 p.m.

March 10, 2004

The Joint Committee on Executive Budget Act Revisions met Wednesday, March 10, 2004, at 8:30 a.m. in Room 421 of the Legislative Office Building. Co-chair Jim Crawford presided. Four Senate members and three House members were in attendance.

The Co-chair called the meeting to order and acknowledged the Committee members and staff members.

The first order of business was a presentation by Karen Hammonds-Blanks, Fiscal Research Division, *Administration and Execution of the Budget: Overview of Requirements and Practices*.

Following the presentation, members questioned staff about appropriations from the General Fund of the State for the maintenance of the State departments and institutions. They specifically asked if the Council of State was included, who decides how federal money is spent, and can the process of the line item budget be changed. Staff suggested that a broader look should be taken at receipts and expenditures. Concern was expressed as to how this would work in the subcommittees. Senator Hagan expressed concern with over expenditures, G.S. 143-23(al)(3), which allows agencies to do what they want. She would like to see it rewritten or deleted. It was agreed that there is too much flexibility in transferring money from one agency to another. How often are agencies audited and can agencies move money around for workers compensation were also concerns. It was suggested that language be changed in G.S. 143-16.3 concerning lapsed salaries. Finally, a discussion was held concerning the role of Government Operations (G.S. 120-76). Representative Sherrill asked if Governmental Operations should be a part of Executive Budget Act.

After a short break, Mr. Ron Snell of the National Conference of State Legislatures was introduced to give a presentation on *The Governor's Authority Over the Enacted Budget in North Carolina and Other States*.

Charles Perusse, Deputy State Budget Officer, Office of State Budget and Management was the next presenter. Mr. Perusse discussed the allotment process, budget management and execution, and adequacy and workability of current law. He asked that members be careful in "tinkering" with the Executive Budget Act.

The Committee recessed for lunch and resumed the meeting with a presentation of *Potential Revisions to the Executive Budget Act and Budget Administration and Execution* by the Fiscal Research Staff. After much discussion, the Committee agreed with staff that much of the language in the current Executive Budget Act needs revising and would use the draft state budget act working copy to make the necessary changes. The Committee members asked staff to prepare changes in the form of amendments to the working document and present them at the next meeting. It was decided that an extra meeting of the Committee was needed. The members decided to meet again on March 29, 2004, at 9:00 a.m. in Room 421 of the Legislative Office Building.

Follow-up questions from the January meeting were presented and explanations were given to the members by Jennifer Hoffman, Fiscal Research Division.

The Co-chair adjourned the meeting at 3:13 p.m.

PRELIMINARY FINDINGS AND RECOMMENDATIONS

The Joint Committee on Executive Budget Act Revisions makes the Preliminary Findings and Recommendations as listed below.

Findings

Finding 1. Consistent with conclusions reached in previous studies, and as supported by testimony presented to the Joint Committee, the Joint Committee confirms that the Executive Budget Act fails to present material in logical order, contains extraneous and obsolete sections, omits definitions of critical terms, and lacks a needed connection with modern fund accounting.

Finding 2. Current budgeting and appropriations practice focuses legislative attention on expenditures supported by the General Fund, while frequently de-emphasizing or ignoring spending from special revenue funds or proprietary funds and expenditures supported by departmental receipts.

Finding 3. The current legal framework for capital planning is the Capital Improvement Planning Act, Article 1B, Chapter 143 of the General Statutes, which lies outside the Executive Budget Act. Although enacted in 1997, the requirements of the Capital Planning Act have not been met. Further the current law does not address budgeting, financing and management of capital improvement projects.

Recommendations

The Joint Committee on Executive Budget Act Revisions is considering legislation that addresses many of the deficiencies presented above and may recommend legislation to be introduced in the 2004 Regular Session for consideration by the General Assembly. The proposed legislation should not disturb the constitutional distribution of authority that now exists between the executive and legislative branches; nor should it modify the budget flexibility granted over the years to the University of North Carolina System. The proposed legislation should provide a more understandable framework within which these topics might be addressed by future legislative bodies.